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Ian Kumekawa, *The First Serious Optimist: AC Pigou and the Birth of Welfare Economics*, Princeton NJ: Princeton University Press, 2017, pp x, 332, hbk, isbn 978-0-691-16348-2, £27.95

In 1920, the year in which his most important work, *The Economics of Welfare*, appeared, Arthur Cecil Pigou (1877-1959), Professor of Political Economy in the University of Cambridge (1908-43), arguably was the most influential economist in the world. Leaving aside his important service to the teaching of economics and his being what would now be called a public intellectual, Pigou made important theoretical contributions to a wide range of topics. But it is on his formulation of the economics of piecemeal intervention, and in particular of the concept of the externality as a rationale of such intervention, that his contemporary significance, and interest to the readers of this journal, rests. Economists had, of course, been concerned with social problems prior to Pigou – his predecessors in the 'Cambridge School' of economics, Henry Sidgwick (20) and Alfred Marshall (29), were prominent in this regard - and previously had reasoned on the basis of something like the externality – Adam Smith certainly did so. But it was Pigou who placed all this on a unified theoretical basis, which, in part because of the influence of his usage, is now known as welfare economics.

The terms in which Pigou formulated the externality, of a divergence between the private and social net products of an investment, has fallen into desuetude, and not only is none of the modern terminology of welfare economics – social welfare function, social cost, market failure, public goods, indeed the externality itself – due to Pigou, but those economics were developed in ways which often treated his specific approach as obsolete (163-64, 199).

As economists generally are an illiterate lot, being much mentioned but little read by them is a very common fate, but Pigou shared it profoundly. When in 1960, the year after Pigou's death, Ronald Coase's vehement criticism of the 'Pigouvian tradition' in 'The Problem of Social Cost' appeared, Coase was directing his fire at a tradition he by then saw as 'largely … oral'. Paradoxically, Coase's criticism, which placed Pigou at the centre of economic arguments for intervention which had long made but gestural reference to him, has been the main impulse to the current recognition of Pigou's importance.

The book under review does not make much of this, but when seeking to establish Pigou's contemporary interest it does emphasise the establishment in 2006 of 'the Pigou Club' of academic economists and, more importantly, powerful public figures who advocate what they claim are Pigouvian interventions which reverse a former period of unwise deregulation (4-5, 209-10). The member of the Club who will be best known to the readers of this journal is Richard Posner, but whilst Posner's membership shows the extent to which the nonsense of deregulation is being abandoned by some of those most responsible for inflicting it upon us (Alan Greenspan is also a member of the Club!), there typically is no real engagement with the detail of Pigou's ideas, his name largely serving to give rhetorical strength to vague tax proposals, with many of which it is difficult to think he would have agreed.

However this is, the revived interest in Pigou has been marked by the appearance of the book under review, the second of only two full length biographies of Pigou to appear in English (a Japanese book published in 2007 which I understand has some biographical material remains untranslated), both within the last three years. The other book, Nahid Aslanbeigui and Guy Oakes' *Arthur Cecil Pigou* (2015), though it is by no means confined to economic theory, discusses Pigou's economics, including the economics of the externality, more extensively and at a generally more sophisticated level than the book under review.

Your reviewer recommends Aslanbeigui and Oakes to those who wish to engage with the issues at this level. But Kumekawa's account of Pigou's personal experience of success and failure in his attempt to bring economic theory to bear on public policy formulation will, however, be of greater direct interest to the readership of this journal.

Kumekawa's title adopts an observation made in an informal note by Joan Robinson, who became a distinguished colleague of Pigou's, which Kumekawa appears to have identified through archival research (131). Pigou was the first serious optimist in that he held out the promise that a theoretically sound economics could guide government action in a way which would significantly improve upon the results of *laissez faire*. Pigou came from a very comfortable, upper middle class family and, after Harrow, went up to King's College, Cambridge, where he excelled as student and don, remaining there, after a little awkwardness securing a fellowship (30-31), for the rest of his professional life. Kumekawa convincingly shows that, with this background, it was natural that Pigou should have adopted the 'social' or 'new liberal' political philosophy which the guided the transformation of British capitalism through extensive welfare reforms under Lloyd George (39). Pigou combined a genuine ethical commitment to the welfare of the less advantaged (49-57) with both a sceptical attitude about the capacity of '"men in the street" to whom he had long condescended' (91) to make correct choices when left to their own devices (81) and a faith in the capacity of expert economists as 'noble scientists' (48) to make better choices on their behalf (32). It was on this basis, which Kumekawa, adopting an interesting coinage of Bernard Williams, calls 'government house utilitarianism' (78- 82), that, in the period around the appearance of the first edition of *The Economics of Welfare*, Pigou wrote on social problems (92-94) and took his place on a number of important government inquiries (97-107).

The theoretical interest in this is that Pigou took a form of the stance one *must* take if one is to put forward welfare economics arguments for intervention. Regardless of the particular economic theory which informs it, intervention analytically rests on the outcomes of voluntary choices in the market being judged from an hierarchically superior viewpoint, and, if the assessment is to some degree negative, action designed to alter those outcomes being implemented. The 'public interest' perspective on which intervention is based *has* to be the perspective of the state, or, to speak precisely, those in which state power to decide in the public interest is vested. Intervention requires some claim of a superior ability to decide, and all that distinguished Pigou's optimistic belief in the superiority of expert economists was its period quality of frankness about this.

But in the second part of his career, Pigou, strange to relate, became a 'serious recluse' (2) who withdrew from public engagement into 'ivory tower' scholarship (111). Kumekawa gives a number of reasons for this, including the degenerating health of a formerly very active man (116) and the impact of the Great War, in which Pigou would not fight but gave distinguished service in the ambulance corps (89), on his morale (87). But, whilst maintaining a sensible proportion about this (128-29), Kumekawa rightly emphasises the way that Pigou's reputation and influence, in Cambridge (151-52) and more widely (135), was eclipsed by that of his former student and junior colleague (149) JM Keynes, who, of course, could well be the economist of greatest historical importance who has ever lived other than Smith and perhaps Marx. This was not because Keynes put forward a rival theory of piecemeal intervention; indeed he famously dismissively denied that the issues addressed by Pigou 'seriously' affected welfare. As it happens, Keynes set up his argument for overall macro-economic management in *The General Theory* by an undoubtedly unfair attack on a 'classical' approach to which he claimed Pigou, in work other than on the externality, had subscribed (141, 148-49). But this was of less significance than that Keynes was to the forefront of shifting the central concerns of economic policy-making in a way which left Pigou somewhat stranded (182), with Pigou's attempts to respond to the new concerns not really having much impact (178). Having noted that Pigou was the first serious optimist, Robinson concluded that the promise of this optimism was realised, not by Pigou himself, but by Keynes (145). But the reason for Pigou's later reclusiveness on which Kumekawa sheds important new light was his disillusionment with the policy process as he had himself experienced it.

One must read chapters 5 and 6 in their entirety to appreciate the atmosphere that is built up by Kumekawa's account of Pigou's sometimes 'striking' degree of disengagement from policy-making in which he was nominally involved (100). Nevertheless, certain themes can be singled out. Pigou came to feel he was merely a figurehead, his opinion not being given much weight (106-107) by politicians seeking to exploit economic ideas for their own purposes (108-109), or by bureaucrats whose competence and independence were questionable (109). All this, Kumekawa tells us, led Pigou to abandon optimism (171) and turned him 'from a believer in the capabilities of governmental administration into a sceptic' (95) who sought refuge from such administration in academic reclusiveness.

A reviewer is obliged to note what seem to be some lacunae in this book judged as biography. Though Kumekawa repeatedly makes critical observations on Pigou's later behaviour (175, 196), he does not convey just how eccentric that behaviour was described in contemporaneous accounts of it. Kumekawa also gives scant attention to the rumours of scandal which have attended Pigou's career, about (disregarding what seem to be groundless claims of association with the Cambridge spies) the way he was appointed to his chair (58-59), an extraordinary difficulty in relations with women, and homosexual relationships with his students (38-39, 86-87). It cannot be denied that these parts of Pigou's life could have had an enormous influence on Cambridge economics, and so they are worthy of the (generally favourable to Pigou) attention they have received from Aslanbeigui and Oakes in their book and elsewhere. But these things will be of little interest to the readers of this journal.

In contrast, Kumekawa's main concern with the biographical detail of Pigou's disillusionment with the policy process will be of great interest. Kumekawa attempts to relate this to some important reservations about governmental regulatory capacity to be found in Pigou's writings on intervention (108-109). The principal shortcoming of Kumekawa's book is, however, that this attempt fails to fully explore the implications of Pigou's personal experience for his argument for intervention and Coase's criticism of this argument, though this is, I repeat, where Pigou's contemporary significance, especially for the readers of this journal, lies.

Kumekawa's treatment of Coase's criticism is very brief and, I am afraid to say, otherwise inadequate. He claims that Coase argued 'that externalities arose not from a major divergence of public and private interests, but because of barriers to negotiation and poorly defined property rights' (208). This account hints at the Coase Theorem, but this has not been the basis of a proper understanding of Coase's thinking for at least 25 years, during which time Coase himself was the Theorem's strongest critic. Coase by no means believed that private property rights solutions could be found for all or even many of the problems welfare economics has identified as externalities. Rather he believed that the externality had had results 'which have been wholly unfortunate' because it is a completely misleading way of identifying the occasions for intervention. It is not possible here to go through all the reasons Coase gave for this belief. The one which will be of most direct interest to the readers of this journal is the following.

Pigou's case for intervention, Coase argued, rested on the logical fallacy that identification of an externality itself justified intervention. In itself, this is never enough. It is also necessary to show that intervention will produce a superior level of welfare. This second stage of the argument was, Coase argued, often ignored because it was assumed, rather than properly argued, that public institutions necessary to successfully carry out the intervention could be made to work as envisaged. Coase called policy made on the basis of this assumption 'blackboard economics': the policy will work on the blackboard; unfortunately it may not be able to be put into practice. Proper choice of economic policy required, *inter alia*, a concept of 'government failure' to balance the concept of market failure which Pigou had made central to welfare economics.

Recent scholarship, to which Aslanbeigui and Oakes amongst others (including your reviewer) have contributed, shows that Coase was, in an important sense, wrong about this. Throughout his work, including in *The Economics of Welfare*, Pigou explicitly states that identifying an externality does not necessarily mean that one should intervene. It raises only a *prima facie* case for intervention, and this case could 'become more than … *prima facie*' only after consideration of 'the qualifications … which governmental agencies may be expected to possess for intervening advantageously'. Furthermore, Pigou certainly was conscious that such agencies could have their shortcomings. The problem remains, in your reviewer's opinion, that Pigou's evaluations of these agencies are always so uninformed as to be merely gestural. It is as if having entered a *ceteris paribus* acknowledgement of the difficulties of a proposed intervention allows one to then proceed with the original proposal. This *ceteris paribus* argument has become a characteristic feature of public policy.

It seems most likely that Coase wasn't even aware of Pigou's *prima facie* case argument when he wrote *The Problem of Social Cost*. Though this does not excuse this fault, Coase later revised his criticism of Pigou in order to show that what he had earlier said was nevertheless 'essentially correct', and your reviewer finds this revised criticism convincing, though Aslanbeigui and Oakes and other contributors do not. Coase showed that Pigou made some truly embarrassing mistakes about the agencies he put forward as having regulatory competence and drew the conclusion that these howlers could only occur because Pigou did not have 'any real interest in the subject'. Where one stands on the typical quality of the assessment of regulatory capacity in public policy proposals will do much to determine one's opinion of the value of intervention.

Though this will not have been Kumeka's intention, he reinforces the impression left by Coase that Pigou was insufficiently interested in analysis of government capacity. Kumekawa's description of Pigou's growing disenchantment with involvement in the policy-making process that led him to withdraw from it does not redound to Pigou's credit, for surely he should have taken his experience into account as he continued to make interventionist proposals in his theoretical work. It would seem he did not.

Though there is an 'epilogue' which brings the story up to date with the recent change in Pigou's fortunes marked by the establishment of the Pigou Club, Kumekawa's book naturally concludes with 'A Redemptive Conclusion', a final chapter entitled 'To "Really Do a Little Good"' (194). Summing up themes which had emerged in the penultimate chapter, Kumekawa tells us that in the fifteen years or so that remained to Pigou after he retired from his chair he regained much of his optimism (200) as he reflected with satisfaction on the unfolding achievements of the post-war Labour Government, which seemed to redeem his earlier faith in state action (201).

If this is so, then the contrast with Coase, who in 1951 left the UK for the US in part because of "a lack of faith in the future of socialist Britain', could not be more marked. Your reviewer, however, finds Kumekawa's conclusion thin and unconvincing. Pigou, we are told, moved from the paternalist Liberalism of his earlier views (and a concomitant scepticism about the Labour Party (173)) to a 'more democratic' belief in the 'competent intervener [which] reflected Labour's vision of a just future based on equality, not mere management' (206-207). Kumekawa surely here underestimates the new liberal influence on the post-war welfare state, having particular difficulty with Beveridge (52, 94, 186-87); and overestimates the democratic commitment of the post-war Labour Party, which previous authoritative accounts described, to cite one such endorsed by Middlemas in his magisterial work, as ‘led by an alliance of Oxbridge intellectuals and TUC oligarchs [who, committed] as they were to working class welfare … had no interest in redistributing [authority, and whose] ethos … was managerial’. Kumekawa also fails to capture the extreme political compromises made by the Attlee Government, traumatically signalled by Bevan’s resignation over prescription charges. What is more, he seems unaware that, the Attlee Government losing power in 1951, Pigou lived out most of his life after retirement from his chair under Conservative Governments and that the Prime Minister when Pigou died was the ideal type of a Conservative patrician whose views, formed under the influence of Lloyd George, were an attempt to bring new liberalism into the post-war era in the form of a ‘middle way’ as scornful of socialism as the Attlee Government understood it as the ‘third way’ of Blair and Mandelson that later sought to root out such socialism from the Labour Party.

That, as Kumekawa’s claims (201), the post-war Labour Government was ‘on some level’ a ‘vindication’ of Pigou’s views can be so only if that level was one of a vague generality (187) comparable to the vindication of those views now claimed by the Pigou Club. And this, surely, indicates the shortcomings of the Pigouvian tradition, in which simply shabby cases for intervention are now normal, and piecemeal intervention is now so common that it is no longer piecemeal. It is ironic that Coase’s criticism of Pigou for making arguments which have led to excessive intervention is, in effect, the basis of Kumekawa’s and the Pigou Club’s defence of him. In this way, this good and interesting book ends on a note of its own unconvincing optimism which unbalances its instructive account of the personal experience of public policy formulation of a figure who has done much to give us the state we now have.